BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2002-63-G - ORDER NO. 2003-15

JANUARY 28, 2003

IN RE:	Application of Piedmont Natural Gas Company, Inc. for an Adjustment of its Rates and Charges and for Approval of Revised Depreciation Rates.	))))	ORDER DENYING PETITION FOR RECONSIDERATION

This matter comes before the Public Service Commission of South Carolina (the Commission) on the Petition for Reconsideration of Order No. 2002-761 filed by the Consumer Advocate for the State of South Carolina (the Consumer Advocate). In addition, Piedmont Natural Gas Company, Inc. (Piedmont or the Company) has filed an Answer to the Petition. Because of the reasoning stated below, the Petition is denied and dismissed.

First, the Consumer Advocate states that this Commission erred in rejecting the Consumer Advocate's weather normalization adjustment resulting from the use of a three-year observation period. The Consumer Advocate states that the Commission's decision to normalize gas volumes based on its historic 12-month test year methodology is arbitrary, capricious, an abuse of discretion, and is not based on substantial evidence in the record. Further, the Consumer Advocate states that the Commission's decision is not based on substantial evidence in the record because "both PSC Staff and Piedmont admitted that the method proposed by the Consumer Advocate's witness Watkins would lead to a more accurate analysis if usage trend analysis would also be introduced into the analysis." The Consumer Advocate then proceeds to quote language from both the Commission Staff and Company witnesses which purportedly admits the propriety of the Consumer Advocate's position.

In actuality, a full review of the testimony presented shows that both witnesses criticized and ultimately rejected the Consumer Advocate's methodology and in its place recommended the method actually utilized by Piedmont and adopted by the Commission. See Tr., Vol. II, at pp. 606-608 and 690-691. The Consumer Advocate's assertion to the contrary is simply not supported by the evidence of record.

Whereas it might be fair to say that all witnesses agreed, all other things being equal, that more data points for this type of analysis would be better than fewer data points, Piedmont witness Fleenor clearly stated that all things were not equal. In rebuttal testimony, and under questioning by one of the Commissioners, Fleenor unequivocally stated his belief that the longer test period advocated by Consumer Advocate witness Watkins created significant risk that additional variables other than weather, including declining per customer usage, could inaccurately impact the single variable linear regression weather normalization calculation. See Tr., Vol. I, at pp. 164-167 and Tr., Vol. II, at pp. 690-691. Witness Fleenor's concerns were supported by a long-term GRI study offered into evidence by the Consumer Advocate and admitted into evidence as late-filed Hearing Exhibit No. 7. In Fleenor's view, this risk was minimized by using a shorter 12-month period consistent with the Commission's historic approach to normalization. Staff witness Sires agreed with Piedmont's approach. See Tr., Vol. II, at pp. 606-608. In summary, the Consumer Advocate's contention that all parties agreed with witness

Watkins' approach to normalizing test period volumes for weather was superior to that proposed by Piedmont and approved by the Commission is contrary to a reasonable interpretation of the evidence and provides no basis upon which to reconsider our previous findings on this matter.

Next, the Consumer Advocate also attacks this Commission's weather normalization methodology based on Piedmont's alleged failure to provide a mathematical analysis of the impact of the trend on declining per customer usage. This argument misapprehends the purpose of Piedmont's testimony. The primary task undertaken by the Company in this area was to provide a mathematical basis for normalizing test year data for variances from normal weather. Piedmont conducted the analysis using 30 years of weather data for determining what is normal and then compared that normal weather to test year weather data. See Tr., Vol. 1, at 63. The study was performed using a linear regression analysis. Piedmont did not attempt to conduct a comprehensive mathematical analysis of every other possible independent variable which might impact such an analysis. Instead, and because all parties agreed that weather is by far the largest independent variable in gas volume fluctuations, Piedmont sought to minimize the impacts of other variables changing over time by utilizing a 12-month test year method. This approach is rational, consistent with our historic practice, and is supported by the evidence in this case, as well. It is also consistent with the method adopted by Consumer Advocate witness Watkins in Piedmont's last South Carolina rate case.

While the Consumer Advocate's own evidence in this case indicates that declining per customer usage is a trend in this region of the United States, the discrete impact of that trend is not known with precision. This uncertainty is one factor which has prompted us to select the 12-month test year method in this case, and to pursue this matter, if at all, in a separate proceeding, so that a broader and more complete analysis of the trend can be undertaken.

In addition, the Consumer Advocate states a belief that our Order No. 2002-761 erred in relying on its established practice for normalizing gas volumes for the effect of weather. In support of this assertion, the Consumer Advocate cites Hamm v. South Carolina Public Service Commission and South Carolina Electric & Gas Co., 309 S.C. 282, 422 S.E. 2d 110 (1992) for the proposition that a previously adopted Commission policy may not furnish the sole basis for Commission action. Although the case cited by the Consumer Advocate certainly stands for the legal principle stated, the case has no real relevance to the Commission's action in this Docket. In actuality, we relied on a substantial number of grounds in adopting the normalization procedure proposed by Piedmont, as is apparent from the several pages of discussion on this issue that appear in Order No. 2002-761. Only one of these grounds was the fact that Piedmont's method was consistent with the method historically utilized by the Commission. In light of the substantial basis for the Commission's decision on weather normalization, discussed in greater detail in a later section of this Order, the Consumer Advocate's claim of error based on the Commission's purported "sole reliance" on its established practice is without merit.

Finally, the Consumer Advocate criticizes the Commission's Order on the grounds that the Commission erred in determining that a separate study might be appropriate before changing methodologies and that its decision was consistent with the manner in which Piedmont calculates R factors under the Weather Normalization Adjustment formula. The first argument both misconstrues the Commission's Order and misstates the Commission's findings.

In the first instance, the Commission's Order clearly says that "[e]ven if the Commission had concerns about its present policy of using a 12-month test period for weather normalization purposes, the Commission is not convinced that it should make changes in this proceeding for at least two reasons." In this case, this Commission is not ordering or finding in its Order that a separate study be conducted. To the contrary, the Commission is simply identifying an additional barrier to adoption of the change in weather normalization methodology proposed by the Consumer Advocate in this case. Obviously, the identification of reasons why the Commission would not approve the methodology proposed by the Consumer Advocate, in addition to the reasons underlying the Commission's adoption of the method proposed by Piedmont, does not provide any basis for reconsideration of the Commission's holdings on weather normalization in this case. Second, this Commission's recognition that adoption of a three-year test period for rate case weather normalization would be inconsistent with the period utilized by Piedmont in establishing year-to-year weather normalization adjustments is not improper. While the Consumer Advocate argues that no one submitted evidence on how these R factors would be impacted by an adoption of a three-year normalization test period, the fact remains that these two "weather normalization" periods would be inconsistent. There is nothing erroneous about this Commission's reference to such inconsistency in our Order.

It should be noted that we identified a number of bases for our determination to utilize a 12-month test period method for purposes of normalizing gas volumes for weather in Order No. 2002-761. These included: (1) evidence submitted by Piedmont in the form of testimony by witness Fleenor and the Consumer Advocate in the form of the GRI study which demonstrated greater risk of normalization error due to factors other than weather when utilizing a three-year period compared to a 12-month test period; (2) evidence submitted by the Commission Staff and the Company in support of a 12-month test period; (3) consistency in utilizing a 12-month test period for normalization purposes with the test period data utilized by the Commission with respect to all other aspects of setting rates; (4) consistency with the Commission's previously approved method of normalizing gas volumes for weather; (5) inconsistency between the Consumer Advocate's position and Consumer Advocate witness Watkins' testimony in this case and in Piedmont's last rate case on this issue; (6) consistency with the method utilized by Piedmont to set R factors in conjunction with its Weather Normalization Adjustment formula; and (7) concerns over potential difficulties that could result from changing methodologies in this company-specific proceeding. This Commission discussed each of these issues and cited the evidence supporting each in approximately six pages of written discussion in our Order. Each of these factors supports our determination to utilize a 12-month test period for normalizing gas volumes.

The weather normalization issue is a complicated one. The Commission had before it two methods of adjusting test year consumption to normal weather based on a 30 year average. The Company used test year data in making this normalization adjustment, while the Consumer Advocate used test year data, plus data from the two prior years. In all prior decisions, this Commission has utilized the test year data in making this normalization adjustment. This has been true for Piedmont, as well as for other local distribution companies providing retail gas service in South Carolina. To change this methodology in isolation during this rate proceeding would not be the appropriate thing to do.

The method using test year data demonstrates that the test year was warmer than normal. Similarly, the use of three years data as proposed by the Consumer Advocate demonstrates that the Consumer Advocate's review period was warmer than normal. Clearly, both methods have merit and have reached the same conclusion that the test year was warmer than normal. The difference in methods is just how much warmer than normal the test year was.

In continuing to support Piedmont's methodology, this Commission understands that as we are setting rates for future usage, our estimates may not accurately predict future revenue streams, because weather is a tremendous factor in gas sales. However, we do have a system of checks and balances already in place to monitor this situation. If the Company has revenue streams over and above what is contained in our original decision, this will lead to additional profits. If those profits reflect earnings in excess of the authorized rate of return, the Commission will have an opportunity to make necessary rate adjustments on a quarterly basis.

In any event, we reject the Consumer Advocate's allegations of error in regard to our adoption of weather normalization principles as propounded by Piedmont, because of the reasoning as stated above.

The second major issue raised by the Consumer Advocate is our approval of a 12.6% rate of return on common equity for the Company. According to the Consumer Advocate, our finding is arbitrary, capricious, an abuse of discretion, and is not based on substantial evidence. This comes as somewhat of a surprise to us, since our finding of 12.6% as the proper rate of return on equity was based on the testimony of a witness for the Company, Dr. Donald Murry. Dr. Murry recommended 12.6% as the proper rate of return for Piedmont, which, in our opinion, was substantial evidence to support our conclusion. However, further explanation follows.

The Consumer Advocate cites three grounds upon which he contends that the Commission's allowed rate of return on common equity is in error in this case. First, the Consumer Advocate contends that Piedmont effectively withdrew its proposed 12.6% return on common equity proposal in conjunction with the filing of the Company's Proposed Order in this case. Second, the Consumer Advocate contends that the evidence supporting the Commission's determination on return on common equity is flawed. Third, the Consumer Advocate contends that the Commission failed to make adequate findings to support its return on common equity finding. Unfortunately for the Consumer Advocate, none of these contentions are supported by a reasonable view of the evidence or the proceedings in this docket, and none provides any basis upon which to modify or amend the Commission's determination that an allowed rate of return on common equity of 12.6% is just and reasonable in this case.

First, the assertion that Piedmont effectively withdrew its proposed 12.6% return on common equity in conjunction with its filing of its Proposed Order in this case is without merit. Piedmont's Proposed Order did state that the reasonable rate of return on equity in the case was 11.525%. See Piedmont Proposed Order at 74. There was a cover letter attached to that Proposed Order which contained language that requested that we "adopt the various Piedmont positions set forth in the proposed order, including but not limited to its position on rate of return." However, the letter also states the following: "I have enclosed a schedule illustrating Piedmont's original filing, adjusted for items agreed to by the Company, which reflects a revenue requirement of $13,156,566 compared to the Staff's recommended revenue requirement of $8,896,051." This would indicate to us that Piedmont was discussing its original litigation positions, including its proposal of a 12.6% rate of return on equity. The materials submitted by Piedmont were not sufficient to overcome Dr. Murry's testimony at the hearing, at which time he recommended a 12.6% rate of return on equity.

The Consumer Advocate states that the Company "withdrew" its rate of return testimony by citation of the above-stated language. However, any "withdrawal" is far from clear when we review the Piedmont language contained in its letter. We believe that the language referring to Piedmont's original filing with a revenue requirement of $13,156,566 makes any "withdrawal" in this case ambiguous at best. Further, if the

Consumer Advocate is implying that Piedmont "waived" its right to assert the 12.6% rate of return on equity, it has failed to establish such a waiver. A waiver is a voluntary and intentional abandonment or relinquishment of a known right. Maxwell v. Genez, 350 S.C. 563, 567 S.E. 2d 496 (Ct. App. 2002). Further, the party claiming the waiver has the burden of establishing it. Heritage Federal Savings and Loan Association v. Eagle Lake and Golf Condominiums, 318 S.C. 535, 458 S.E. 2d 561 (Ct. App. 1995). The assertions made by the Consumer Advocate do not convince us that the Company intended to waive its presented testimony. Again, the language in the transmittal letter is ambiguous at best. Without any other evidence, we do not believe that a waiver has occurred.

In addition, one of the major purposes of a brief or proposed order is to allow the parties to argue their positions in a particular case. See 26 S.C. Regs. 103-875 (C)(3)(1976). However, we do not believe that the brief or proposed order and/or its accompanying documents such as a transmittal letter rise to the same level of credibility as sworn testimony presented before this Commission. The material cited by the Consumer Advocate is simply an unsworn transmittal letter and proposed order from counsel for the Company. Further, we do not believe that these documents can counter or waive said testimony unless said material clearly establishes the waiver. A waiver must be established by clear and convincing evidence. See Wainscott v. Dunn, 1994 WL 732093 (S.C. Com.Pl., 1994). Although we understand the Consumer Advocate's argument in this case, we simply do not believe that the quoted language from the transmittal letter clearly and convincingly establishes a waiver of the conclusions seen in

Dr. Murry's testimony on rate of return on equity in this case. Thus, Dr. Murry's testimony stands.

Second, the Consumer Advocate contends that Dr. Murry's analysis was flawed, and therefore, the Commission could not rely on Dr. Murry's conclusion to support its finding on rate of return on equity. This point is unavailing. The fact that Dr. Murry might have reached a different recommendation on return on common equity, more within the preference of the Consumer Advocate, if he had used a different method applied to different data, is not in any way indicative of flaws in Dr. Murry's testimony or error in the Commission's determination of a just and reasonable return on equity in this case. To the contrary, it simply confirms what is readily apparent from the evidence in this case, i.e. that different experts can reach different conclusions about what constitutes an appropriate rate of return on equity for a natural gas local distribution company even when utilizing similar methodologies. This Commission must weigh all the relevant evidence, as it did in this case, and arrive at a just and reasonable result in its exercise of discretion. This, we did in the present case. We weighed Dr. Murry's testimony against the testimony of the other rate of return witnesses, and, for the reasons elucidated in Order No. 2002-761, found Dr. Murry's analysis to be the most credible. We discern no error. The Consumer Advocate brought some of these alleged "flaws" to the attention of this Commission at the hearing in cross-examination. See Tr., Vol. I, Murry, at 243-286. However, when all was said and done, we still believed Dr. Murry's testimony to be the most credible of the rate of return witnesses, again for the reasons stated in Order No. 2002-761. We sit as the trier of facts, akin to a jury of experts. See Hamm v. South

Carolina Public Service Commission, et. al., Id. In this case, we simply believed Dr. Murry over the testimony of the other rate of return witnesses.

We would further note that, in these uncertain financial times, it is imperative that this Commission send the proper signals to the financial community with the adoption of Dr. Murry's testimony. This, we clearly did in the present case. To take any other approach would clearly be to the detriment of the Company's ratepayers.

Lastly, with respect to the argument that this Commission failed to make specific findings on the testimony of Staff witness Spearman, the Consumer Advocate overstates the Commission's obligations. While it is true that this Commission must fully explain its findings on allowed rates of return, that obligation does not require a specific factual finding on every single aspect of the evidence. The test is whether the Commission has fully explained its findings and the evidence upon which it is based. This we did in much detail in Order No. 2002-761.

In sum, there is no merit to the Consumer Advocate's argument that the Commission erred in adopting an allowed rate of return on common equity of 12.6% in this case. None of the Consumer Advocate's contentions as explained above support any modification of or adjustment to the Commission's prior determination of a just and reasonable rate of return on common equity of 12.6% in this proceeding.

Having fully discussed the Consumer Advocate's allegations of error above, we hereby deny and dismiss the Petition for Reconsideration.

This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Mignon L. Clyburn, Chairman

ATTEST:

Gary E. Walsh, Executive Director

(SEAL)